

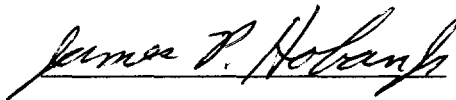
The Changing View of Pensions

An Honors Thesis (HONRS 499)

by

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A handwritten signature in cursive script, reading "James P. Hoban", written over a horizontal line.

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### **Purpose of Thesis**

This is a profile of the retirement income system in the United States. The purpose and evolution of pensions throughout the twentieth century, as well as predictions of the future of pensions are discussed. Along with a discussion of the make-up of pensions is an exploration of the possible effects of pension growth on the economy, personal savings, and labor markets in the United States. Finally, issues in pensions are discussed, including misuse and mismanagement of pension funds as well as other ethical issues regarding pension funds.

From the invention of the "horseless carriage" to human space travel, the twentieth century has shown to be a period of great change in America. One particular area of change affects millions of average Americans every day, even if little thought is given to the subject; that area is the changing profile of retirement income. While many people will not be physically or mentally able to continue to work their entire lives, it is presumed that those who can do not **want** to work their entire lives. Therefore, retirement income becomes important to each of us when considering the need to financially provide for ourselves in our golden years.

For several years, the pattern in American families was for the head of the household to work until retirement and thereafter be supported by a combination of financial assistance from his children and personal savings. The scope of financial security in retirement as the twenty-first century nears is much more broad and diverse. Retirement income today ranges from personal savings accounts to multi-billion dollar federally sponsored programs. Also, as the post-war "baby bloomers" get older, the number of current and potential beneficiaries as well as the dollar amount of their benefits is growing at an amazingly rapid pace.

Along with the changing scene in the area of retirement income come changes in questions of ethics, management and misuse of retirement income funds. These questions concern privately and publicly sponsored funds and personally and professionally managed funds. Another problem associated with the quickly changing field of retirement income is the lack of understanding by the general public concerning the issues that will in fact play an important

role in their own personal lives.

### RETIREMENT INCOME PROFILE

The retirement income system in the United States is an ever-changing entity. Prior to the Great Depression, most people relied on personal savings and family support for financial security in retirement. Organized pension funds, both public and private, can be greatly attributed to the effects of the Great Depression. As Americans saw their current living expenses disappear, personal retirement income saving was rarely practiced. Organized pension saving as well was close to unheard of. Prior to 1940, less than fifteen percent of all private sector employees participated in a pension plan [Andrew, 3]. It was President Franklin Roosevelt's "New Deal" and the Social Security Act of 1935 that marked the beginning of pension growth in the United States. Social Security benefit payments started in 1940 and today, it is a vast, multi-program system which provides financial security to billions of recipients annually.

Far from simply personal savings, benefits to the elderly and retired come from a wide array of sources. (See Figure 1) The largest sector of the retirement income system is the Social Security program. Instituted in 1935, Social Security is a federally sponsored, unfunded pension plan. Currently, approximately fifty percent of all retirement benefits are paid by social security. Also, many people collect both Social Security and private pension benefits. The U.S. Department of Treasury

reports that 31 percent of Federal tax outlays for 1991 were paid in Social Security benefits. An additional seven percent was spent on medical assistance and food stamp programs.

The second largest component of the retirement income system is employer-sponsored private pension plans. Private pensions in particular have grown dramatically over the last fifty years, especially in the last decade. (See Figure 2) Several issues concerning the management, misuse and growth of private pension funds have surfaced in the past two decades and are of major concern. Detail will be given to these issues in a later section.

The oldest component of the retirement income system, personal savings, has changed greatly over the past century but still remains a vital component. As stated previously, prior to the 1930's, personal savings and retirement income were almost synonymous. As a percentage of retirement income, personal savings- once a major portion, has decreased drastically during the post-war era. As organized pension security became readily available to most Americans, personal income was used more for current consumption, thus the decrease in personal savings. However, the personal savings component showed a strong reappearance in the 1980's with the growth of Individual Retirement Accounts (IRA's). The growth of IRA's can be attributed to two factors. First, prior to the Pension Benefit Guarantee Corporation (PBGC), private pension benefits were not guaranteed or insured. The effect of this left several people in the 1970's finding themselves at retirement age, without a job--- and without financial security. IRA's were a way to federally insure savings

for retirement with an added benefit. This added benefit is the second reason for the growth of IRA's in the 1980's, tremendous tax incentives. IRA's provide a way of reallocating personal financial assets such that personal income tax is deferred or reduced. Personal savings in IRA's continue to grow in the 1990's, but the pace is less rapid than the 1980's growth.

Other components of retirement income worth mentioning are public assistance and medical programs. Approximately twenty percent of all retirement income comes from these sources [Andrew, 5]. In 1964 the food stamp program was enacted. This enables elderly people to maintain better nutritional standards than may otherwise be possible. Approximately two million elderly people use food stamps today. Other programs of great significance are Medicare and Medicaid, both introduced in 1965. As a result, virtually all the elderly receive medical coverage. In addition to Medicare and Medicaid, Supplementary Medical Insurance (SMI) is available. SMI covers about eighty percent of all allowable medical and related health services not covered by Medicare and Medicaid, plus an additional \$15 billion in benefit costs annually. In addition to these federally sponsored programs, many elderly take advantage of low income housing and rental assistance programs.

#### GROWTH OF PENSION FREQUENCY

As previously noted, pensions have, and are currently, undergoing major changes. The most notable change in pensions during this century is their enormous growth. The first domestic

pension fund was established in 1875 by the American Express Company [Davey (1), 1]. Growth was slow, and by 1935, only four million workers were covered by pension funds. The huge change came with the decade of the 1940's. This showed to be a major growth period for pensions. The Social Security Act of 1935 not only launched the first government sponsored pension plan, but also encouraged industry to provide retirement benefits for their workers, thereby providing stimuli for growth of pensions in the 1940's. Another stimulus to pension growth during the decade was the imposition of wage controls during World War II. Pension benefits were terrific incentives for employers. First, pension contributions were not considered pay hikes and therefore offered an alternative to wage controls. Pensions were also used as non-pay incentives for employers to attract new employees. Other factors in the decade attributed to pension growth. First, in 1948 the Supreme Court upheld a National Labor Relations Board (NLRB) ruling that pensions are a bargainable issue. This led to employer sponsored pension funds as an added benefit to union employees. Another incident occurred in 1949 when the Steel Industry Fact Finding Board found that the industry is obligated to provide for its workers retirement benefits [Davey (1), 5]. These factors combined led to the explosion in pensions and by 1950, private pension beneficiaries and assets had more than doubled from their 1940 positions [Ippolito, 121].

The next twenty years were periods of continued rapid growth and by 1970, private and public pension assets had reached \$548 billion [Ippolito, 121]. However, pension funds took a turn in the

1970's with the enactment of the Employee Retirement Income Security Act (ERISA) of 1974. Although pension assets continued to grow, the number of employees covered by private pension funds increased at a decreasing rate. "Since the passage and implementation of ERISA, this growth, has slowed at least in terms of workers covered, as thousands of plans- for the most part smaller ones- have been terminated" [Davey (2), 1]. ERISA was enacted to protect the beneficiaries of funds. In some ways it has; but detrimental effects, such as those previously mentioned, also occurred. Although ERISA does not require companies to have pension plans, strict restrictions and requirements make pension more expensive for employers and sometimes return less to the beneficiaries.

#### CHANGES IN PENSIONS DUE TO ERISA

One of the changes that came about due to ERISA is the change in participation. Because of the increased cost that may occur due to ERISA guidelines, many companies choose not to provide pension benefits at all. This usually effects smaller companies. The size of the fund and amount of benefits may also be affected.

Another change is in the funding procedure of pensions. Although many funds are currently still "unfunded," many companies are funding as they go to provide for safer pension benefits upon employee retirement. This is a definite plus for most beneficiaries.

Other changes due to the implementation of ERISA include the PBGC, tighter guidelines concerning the management of funds



(fiduciary responsibilities) and stricter reporting requirements on the performance of fund investments. These affects all provide for a lower degree of risk, but also more expensive management and usually a lower degree of return on benefits. ERISA has had many positive effects on the profile of pensions, but as with most things, the companies and beneficiaries must take the benefits with the added cost.

### **GROWTH OF PENSION ASSETS**

Although the growth of employees covered by private pension fund assets have increased dramatically, this growth in assets has been attributed to many factors. One possible reason is the recent favorable changes in federal tax laws. Another reason that has received much attention is the growth in investment gains--especially in equity investments. Reasons for this growth is two-fold. The first reason is the huge growth in the market returns in the 1980's, even considering the market crash in 1987. The second reason is the growth of equity ownership by pension funds. Pension fund ownership of corporate equities has grown from .9 percent in 1950 to approximately 30.1 percent in 1990. This growth is expected to continue. It is projected that by the year 2000, pensions will own 47.1 percent of all corporate equities and 44.1 percent of all corporate bonds [Ippolito, 124]. It is also projected for the year 2000 that total pension assets will exceed \$2.789 trillion, an increase of 171 percent over pension assets in 1981 in **real** terms. Thus, the effect of pension growth has and continues to play a tremendous role in our economy.

## EFFECTS OF PENSION GROWTH ON THE ECONOMY

One of the most important impacts of pension growth in the past half century is the effect on the economy. These changes effect almost everything from personal savings to capital formation. Particularly in the last decade, pension funds as a percentage of our entire economy have grown too large to be ignored in economic analysis.

One of the largest effects of pension growth is that on the U.S. financial markets. As previously noted, pension fund ownership as a percentage of corporate equities has grown drastically. Approximately one-third of the market is owned by pension funds and is expected to continue to increase. Effects of this growth percentage are three-fold. The first effect centers on the goal of many pension managers- to outperform the market to maximize employee benefits. The effect of this may be encouraged buying and selling of securities to increase return; the problem is greatly increased transaction costs come with the package. Another effect is as pension holdings increase as a percentage of the market, they may own too much of the market to outperform it. Perhaps other investments could provide better return for less risk. The final and more positive effect of increased asset holdings is that the "average" person has access to large capital markets with professional management and increased diversification. The effects of stock market holdings apply for other financial investments as well as equity holdings.

## EFFECTS OF PENSION GROWTH ON PERSONAL SAVINGS

The role of pensions has another impact on the economy which affects the daily lives of Americans, the amount of personal savings. Personal savings, as a result of organized pension funds, has fluctuated greatly over the past forty years as shown previously. However, organized retirement savings, in both the public and private sectors has been growing steadily. In 1957, pension savings amount to twelve percent of a person's wealth on average. In 1980, pension savings increased to twenty percent of a person's wealth. If life insurance reserves are added to this, the percentage increases to approximately thirty-five percent [Tobin, 18]. The question arises, are organized pension savings and personal savings different things? "Pension savings...in some degree serve as substitutes for voluntary individual savings" [Tobin, 19]. The fact is, voluntary savings and compulsory retirement savings have some different characteristics; but, they are **savings**, regardless. If attention is given to savings alone, including compulsory and voluntary savings, an increase in real terms can be seen over the past fifty years. "Many people really do like to be forced to save for retirement. They want to be spared their own temptation to spend" [Gray, 18]. If voluntary retirement savings is the only factor considered, a different conclusion may be drawn. Recent evidence shows that IRA's are not retirement savings at all (for some), but simply a reallocation of existing assets to take advantage of favorable tax laws [Andrew, 127]. The effects of this on the economy has only been speculated upon, but one view states "... then pensions would reduce national

savings. These effects might be quite significant" [Bilow, 81]. Regardless of which way the effects may turn, that the growth of pensions has an effect on personal savings is certain.

#### ECONOMIC CHANGES AS A RESULT OF DECREASED SAVINGS

The effects of the decrease in personal savings has a domino effect on other components of the economy as well. One area that is affected is the labor markets. It has been asserted that as pensions continue to grow, the number of older workers with pensions participating in the work force has declined [Kotlikoff, 283]. The trend has been for people to retire at the normal retirement age for their jobs, neither early nor late. This could be based on one of two probable reasons. The first is as people better financially prepare for retirement, there is greater incentive to leave the workforce at retirement age. The other factor is people have less incentive to retire early. In recent years, the "cost" of early retirement is large cuts in retirement benefits. Therefore, people are retiring closer to the traditional retirement age for their perspective fields of employment.

Another effect on the labor market due to similar reasons as those which effect age is the effect on career mobility. Just as early retirement, premature departure from a company may cause very large pension capital loss [Ippolito, 166]. Pensions represent an incentive tool for employers which helps keep employee turnover very low [Mitchell, 286].

Not only do personal savings affect labor markets; they also affect capital formation in the economy. Organized retirement

investment, whether compulsory or voluntary, puts billions of dollars each year into the economy which leads to higher capital formation. Franco Modigliani asserted and James Tobin re-affirmed that "the entire stock of wealth in the United States could be simply the accumulation of retirement savings [Tobin, 18]. This idea has been challenged by expert economists; however, little doubt remains that the effects on capital markets from pensions are great.

The United States has been criticized in comparison with our Japanese counter-parts for our relatively low personal savings. However, retirement savings is in fact personal savings. The major difference is that investment is made on behalf of the beneficiary rather than **by** the beneficiary. It has been said that "...compulsory retirement saving and voluntary saving is probably no longer a significant factor...people save less in other forms [instead]" [Tobin, 19].

Although national savings do increase with increased pensions, a problem arises because many pensions are unfunded. The largest component of retirement income in the United States- the Social Security system- is unfunded. Very simply put, the retired generation is supported by the working generation and so on. Thus, the contributions made by each person are not invested directly and saved. They are instead used for current consumption by the retired beneficiaries. Economist Martin Feldstein argues that the amount of wealth required to provide benefits for Social Security at the turn of the century will exceed several trillion dollars annually. If Social Security were fully funded, the nation's stock

of production capital would be that much greater [Feldstein, 905]. Similarly, Kotlikoff shows that the Social Security system, as is, attributes to a twenty percent steady reduction in the capital stock [Kotlikoff, 233-53].

Just as Social Security is unfunded, many private pensions are also unfunded. The effects of unfunded private pension funds, although on a smaller scale, are similar to those of Social Security. Other issues pertaining to unfunded private pensions will be addressed in a later section.

As pensions have continually grown and evolved over the last fifty years, the changes shown have been very large. Growth of pensions is expected to continue well into the twenty-first century and its effects can only be speculated. Changes thus far have affected the labor, financial and capital markets, and personal savings. Changes have occurred due to the implementation of ERISA and PBGC which helped to guide the way pensions are funded, managed, and distributed. Other changes in the next few decades are certain to be just as broad as financial innovation and the U.S. economy are constantly changing as well.

#### **PENSION FUND MANAGEMENT**

The management of pension funds has been given considerable attention in the past two decades. Although ERISA provides strict standards for the management of funds, the Pensions Benefit Guarantee Corporation (PBGC) and the Department of Labor take the responsibility of insuring that the sponsoring firm and the pension fund are legally independent entities. Therefore, two main types

of pension plans emerged, trusted and insured plans. Trusted plans are defined as,

...those that are financed through trust agreements that may be either discretionary or directed in nature. Under discretionary arrangements, trustees (ordinarily banks or trust companies) enjoy considerable freedom in the way they invest pension assets; under directed arrangements, trustees act more in a custodial capacity, being responsive to others- independent money managers, for example- in investment matters [Davey (2), 5].

The other main type of pension plan is an insured plan. Insured plans are defined as,

...those that are financed through agreements with insurance companies. Sponsors of such arrangements make periodic contributions which are normally invested at the discretion of the insurance firms that contract to provide pension benefits [Davey (2), 6].

Regardless of who manages the fund, the fund's sponsor often has a basic objective for its investments. Many firms have written policies to guide portfolio goals and investment criteria. Davey says, "Frequently stated investment goals include: preserving capital, maintaining adequate funding, optimizing asset growth..." and others [Davey,5]. Other policies stress the assurance of adequate funding. This concept leads to the controversial objective. This objective for the pension investment policies involves the value of the firm. Unfunded pensions tend to increase the value of the firm, whereas funded pensions are much "safer" for employees. Basically, "...an unfunded pension liability is in essence a firm borrowing from its employees" [Kemp, 33]. This type of policy has been more frequent in recent years since the PBGC was formed. The PBGC serves as a buffer between the company, the fund

managers, and the employees. Employers may feel more free to use pension funds to boost the value of the firm because the risk of doing so becomes lower with pension insurance.

Pension fund managers often rely on very specific investment guidelines, either their own or those specified by the sponsor. These guidelines cover desired risk, return, and asset mix as well as imposing other investment constraints.

Risk guidelines can be stated in qualitative or quantitative terms. These specifications guide managers toward conservative, moderate or aggressive investment practices. Qualitative guidelines include such statements as "a willingness to tolerate some interim fluctuations in the market value and rates of return in order to achieve the objectives," or a more broad example "...and a desire to limit the volatility in the fund's rate of return to a level that is not substantially greater than the average variability experienced by other U.S. retirement plans" [Davey (2), 15]. Quantitative measures are also more commonly used including Beta's, Standard & Poor's bond ratings and mathematical criteria.

Another common investment guideline relates to required rates of return on investment portfolios. As with risk positions, target rates of return can be expressed in qualitative or quantitative terms. Qualitative guidelines for investments regarding rates of return range from such measures as exceeding or meeting the Standard & Poor's 500 return to broad guidelines such as "A highest possible return." Quantitative guidelines, which are used more often, call for specific percentage returns. Examples are



percentage points above the inflation rate and other specific returns in real terms.

The most common investment guideline specifies, or at least directs, the asset allocation mix of the fund's holdings. The asset mix chosen for a fund is likely the best indicator of the sponsor's position on the previous two subjects: risk and return. If a sponsor is willing to sacrifice a measure of safety for a high return, one could expect very high percentages of the portfolio in common growth stocks. On the other hand, if safety is of prime importance, one could expect to see a portfolio high in U.S. treasury security holdings. The trend in the past forty years, however, has been a shift from large percentages of government securities to large holdings of common equity. It seems that insured assets with lower returns are becoming less desirable as we enter the 1990's. (See Figure 3) It is projected that by the year 2000, pensions will hold over forty percent of their assets in corporate equities [Ippolito, 125]. There are several possible reasons for this shift, however a commonly accepted reason is once again the PBGC. As previously asserted, the PBGC serves as a buffer between companies and employees; thus, firms with a higher level of PBGC insurance tend to favor riskier asset holdings [Bodie, 40].

The last common area of investment guidelines are constraints on investment placed by the sponsoring firm. Examples of constraints are limits on amounts of assets to be placed in a single company or industry, maturity limits of securities, required ratings of individual securities and others. Other examples of

investment constraints can be seen in Figure 4. Although investment constraints do exist, many sponsors trust the fund managers to "do what they do best" and provide no constraints at all.

#### **MISMANAGEMENT-MANAGEMENT OF PENSIONS**

Although much attention has been focused on the management of pension funds, much more has been recently given to the mismanagement-management of funds. The Employee Retirement Income Security Act of 1974 provides that administrators manage funds "Solely in the interest of the participants;" the question then arises, what is the "best interest" of the participants? One may assert that the best interest is a safe income awaiting the employee upon retirement while another may argue that a greater amount of wealth with a fair amount of risk is best. Still others may argue that the "best interest" of employees is "the well being of individual workers and their families, not just for today and tomorrow, but over their lifetimes" [Gray, 15]. These different ways of viewing the "best interest" of the beneficiaries lead to broad interpretations of ERISA guidelines, which directly leads to some pension fund mismanagement-management. This concept could promote that companies should invest employee pension funds, or portions thereof, into their own company with the intent of improving profitability thereby serving the interest of the employees through pay increases and other bonuses. This idea of applying pensions to reinvestment in the company supposedly serves the participants through pension contributions. The "interest of

the participants" here again happens to benefit the company as well. Rationale for this is stated by Gray as "If we are unable to produce goods and services which can be sold at competitive prices to make a reasonable profit, our ability to make pension contributions and the value of pension assets will be seriously jeopardized" [Gray, 5]. Acting in the best interest of participants is a very broad guideline which can easily be construed as permission for the company to "**borrow**" employee pension funds to serve the goals of the management and to promote shareholder wealth.

As private pensions subtly borrow employee funds, "states and cities are plundering employee pension funds to ease their budget crises" [Deutschman, 76]. The 1980's were a period of rapid federal, state, and local spending with borrowed money, this trend is continuing in the 1990's. Suddenly, politicians are finding themselves faced with astronomical budget deficits. Government pension funds for public employees look very attractive to politicians trying to balance their budgets. Some states are outright seizing funds from the billions of dollars set aside for public employees. In July 1991, Republican Governor Pete Wilson of California took \$1.6 billion from the California Public Employee Retirement system (CALPERS) to help ease the \$14 billion state budget deficit. State employees were furious. As protest heated, the California State Legislature prevented Wilson from further actions but allowed the \$1.6 billion withdrawal. California's Third District Court of Appeals will decide on the constitutionality of Wilson's act in the spring of 1992. In

another similar incident, Illinois Republican Governor Jim Edgar withdrew \$21 million from the state retirement systems recently. Although the amount is far less than that taken in California, the Illinois state employee pension plan was under-funded to begin with. The Illinois Supreme Court is currently hearing the case.

Other states that are currently using pension funds for their uses are less bold than California and Illinois; the methods most often used are clever accounting and actuarial practices. The most common way states save money is by increasing projected returns of pension asset investments. The fund managers can creatively, and arbitrarily, raise the percentage of expected return on the fund portfolio over the next several years. The next step in the process is to cut required money invested in the funds. "A basic rule of thumb: If you increase the expected rate of capital appreciation by one percentage point over thirty years, an employer can cut current contributions to the fund by twenty percent" [Deutschman, 77]. An example of this type of practice is the state of Missouri in the past few years. The projected rate of return on its state employees pension fund was increased from 8 to 8.5 percent-- the state saved approximately \$20 million in 1991 in reduced pension contributions.

The recent actions of several states regarding pension fund mismanagement-use can only be properly termed **theft!** State and local politicians are getting away with their actions because the general public, the voters, do not really understand the implications of such things as increased projected returns on portfolios and other similar issues. The implication may be that

the taxpayers (present and/or future) may "foot the bill" for these actions. We are continually spending more than is received in revenues. The interest expense of the borrowed funds in the 1980's is due now and the effects of our current actions will greatly affect tomorrow's retired workers.

Several other issues relating to pension fund management have arisen in the past two decades. Pension portfolio management, voting of pension proxies and social investment issues are just a few.

The option of passive versus active portfolio management is a fairly recent issue in pension investing. Prior to the 1960's, passive management was virtually unheard of. However, as the new century approaches, many pension fund managers are moving more toward passive management of funds. Reasons for this vary. First, as pensions hold larger percentages of their portfolios in equities, larger percentages of markets are held by these funds. Therefore, it is becoming increasingly difficult to outperform the market, even with expert management. The second reason for passive management is increasing transaction costs. As transaction costs increase, it is becoming less profitable to buy and sell regularly rather than using a buy and hold strategy. Another transaction "cost" to consider is the high compensation paid to highly qualified portfolio managers. As these costs increase, trustees and insurance companies are finding it better to use a more passive management style. The trend in managing pension funds is toward indexing funds. Indexing ensures returns similar to that of the market as a whole. This can lead to a lower (pre-"cost") return on

the portfolios, but also may lower risk and definitely cost. By the Fall of 1987, indexing accounted for approximately \$200 billion in pension assets [Davey (2)].

Another question concerning management of pensions is that of voting proxies. As pension funds move toward larger percentages of assets in stocks, they also move toward increased voting rights. According to a recent survey of companies, 75 percent of respondents believe voting responsibility (or right) lies with the investment manager, twenty percent favor trustees, and five percent favor managers of the sponsoring firm [Davey, 14]. The problem associated with voting of pension proxies lies with what vote is "appropriate" for the company, managing firm, and most importantly- the beneficiaries. Some voting issues are fairly easy to decide upon for a fund manager because they relate directly to the performance of the security and thus the overall portfolio. These issues include acquisitions or takeovers, and alterations to a company's capital structure. Other types of issues may conflict with company and/or participant values, thus the right to vote a certain way may lead to controversy.

The issue of voting proxies is one of the many topics included in the concept of "social investing." This topic can be defined in many ways, depending on who defines it, but usually involves the idea of promoting the "best interests" of the employee and sponsors in many aspects. One facet of social investing involves investing funds locally. The idea is that local investment will help the employees by improving the local economy. Other social investment issues are very broad and include such issues as union companies

only investing in other union companies, funds only investing in "environmentally responsible" companies and others. Gray states,

...this kind of social investment approach tends to be epidemic. It will not remain an isolated phenomenon. Reciprocities will take hold! If your state [or company] takes action that withholds funds that may otherwise come to mine, mine will do the same to yours. And so on. It's trade protectionism in another form [Gray, 16].

This is just one example of the many controversies that have stirred over the social investment issue. Because it is a relatively new concept, it is expected that this idea will become increasingly popular in the next several years.

The retirement income system itself is vast, complicated, and ever-changing. From its beginning in the United States as private savings and family support, to the first organized fund in 1875, to the huge, multi-billion dollar industry it is today, the retirement income system is itself an entity. It affects most Americans daily, though many are unaware of its power and effects. It affects our jobs, standard of living, savings and spending habits. It is something that each of us needs to be aware of and to plan for. However, no matter how much we hope to predict what the future holds for us, history has shown that pensions are becoming almost too powerful to control. What the future of pensions and retirement income in general will be is purely speculation and educated guesses. Pension beneficiaries and assets are expected to continue to grow at a rapid pace well into the twenty-first century. As the World War II children approach retirement, more assets, management and contributions will be needed to support them in their old age. As pensions continue to grow to meet these

demands, increases in social, ethical and financial problems can also be expected. Aside from what the future of retirement income holds, the present situation is enough for Americans to ponder. Because it affects us all in several aspects, Americans can no longer afford to remain ignorant of the ever-changing and ever-powerful workings and effects of the United States retirement income system.



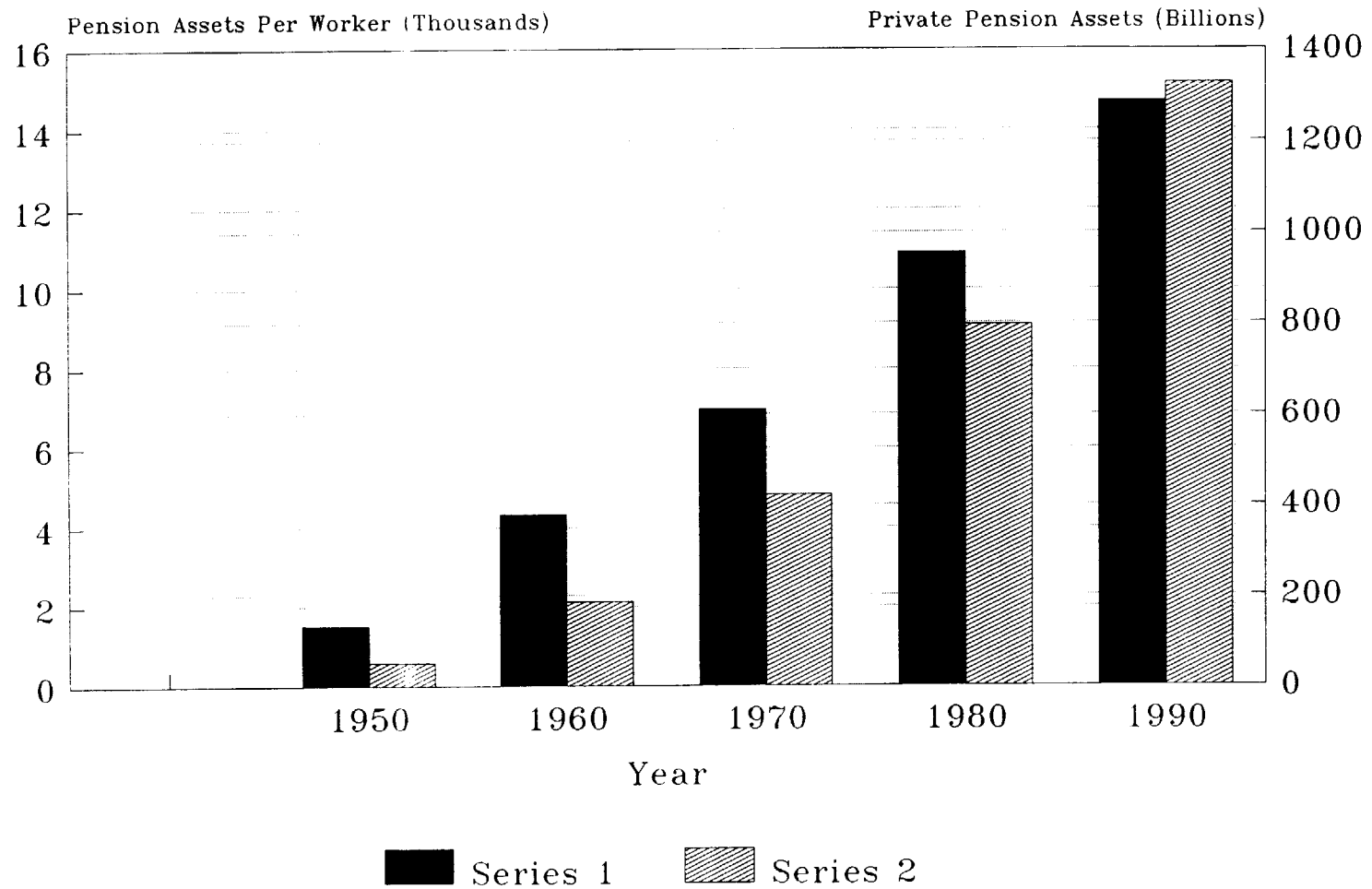
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Figure 1  
The Retirement Income System, 1990

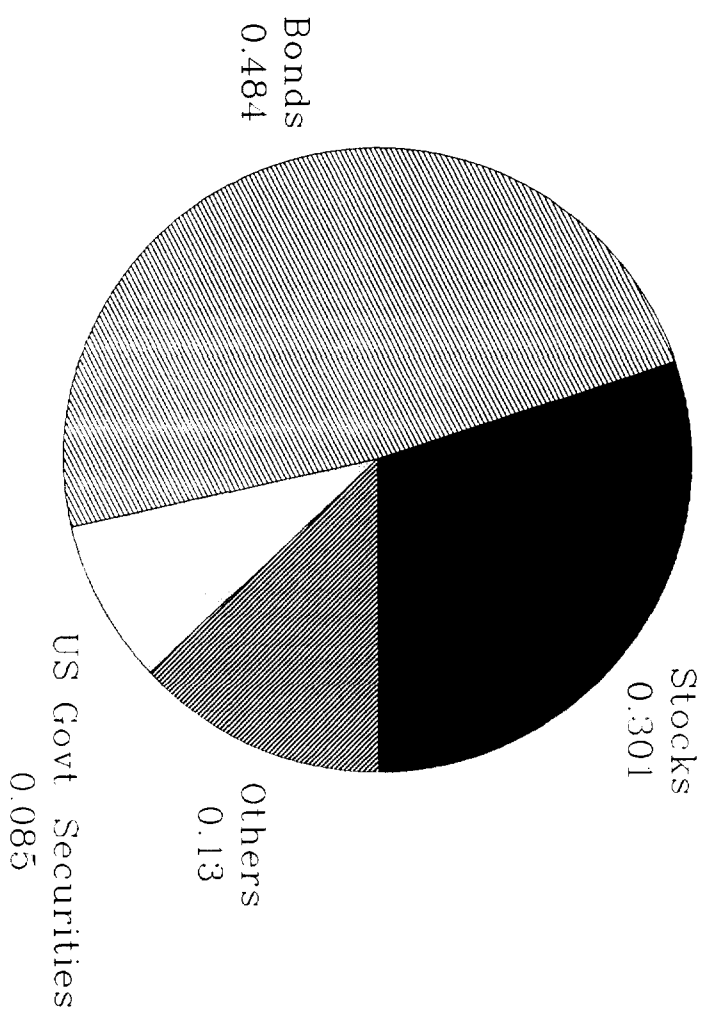
<u>Benefit Type</u>	<u>Beneficiaries (%)</u>	<u>Benefits (%)</u>
Social Security	39.50	48.69
Employer Sponsored Pensions	18.51	29.73
Supplemental Security Income	02.46	00.98
Food Stamps	02.46	00.33
Medicare	65.43	16.67
Medicaid	03.70	03.92
Total	100.00	100.00

Figure 2  
Growth In Private Pension Plans



Sources: Securities and Exchange  
Commission; American Council  
of Life Insurance

Figure 3  
Distribution of Pension Assets, 1990



Source: SEC

Figure 4

Investment Constraints Imposed On Pension Managers

<u>Prohibited Investments or Transactions</u>	<u>Percent of Companies</u>
Securities of Sponsors	19.01 %
Short Sales	15.49 %
Margin Purchases	11.27 %
Letter, Unregistered, or Restricted Stock	8.45 %
Pledging or Hypothecation	5.63 %
Options or Futures	5.63 %
Commodities	5.63 %
Puts, Calls, Straddles or Hedges	5.63 %
Foreign Securities	3.52 %
Warrants	2.11 %
Real Estate	2.11 %
Municipal or Tax Exempt Securities	1.41 %
Other	4.92 %

\*Source: Conference Board Research Bulletin

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